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No. 99-1560

Supreme Court, U.S.
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IN THE
Supreme Court of the United States

INTERNATIONAL PRECIOUS METALS CORPORATION, MULTIVEST, INC., JAMES GROSFELD, INDIVIDUALLY AND AS TRUSTEE OF THE JASON GROSFELD TRUST, MULTIVEST REAL ESTATE, INC., S.S. MELBOURNE, INC., AND THE CYPRESS GROUP, INC.,

Petitioners,

v.

WILLIAM WATERS AND LINDA BARTHOLOMEW, INDIVIDUALLY AND ON BEHALF OF ALL THOSE SIMILARLY SITUATED,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

REPLY TO BRIEF IN OPPOSITION

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CORPORATE DISCLOSURE STATEMENT IN ACCORDANCE WITH RULE 29.6 OF THE RULES OF THE SUPREME COURT OF THE UNITED STATES

The corporate disclosure statement at p. ii of Petitioners' Petition for Writ of Certiorari dated March 22, 2000 is still accurate.

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I. The Court should grant certiorari to eliminate the manipulation of reversionary settlements to enrich class counsel at the expense of their clients.

Respondents advance no legitimate reason to deny the Petition for Writ of Certiorari. Respondents do not challenge the scheme described in the Petition, or that they engaged in each and every element of the scheme. Respondents do not deny that they embraced a reversionary settlement[1] and used it to demand a fee equal to one-third of the gross nominal settlement fund of $40,000,000, *knowing* that only a minor fraction of the class would file qualifying claims (in this case, approximately 5,000 of the 20,600 class members—or 25%—filed qualifying claims). Respondents do not deny that they *knew* their fee demand of $13,333,333 would yield a fee of more than 200% of the actual class distribution of approximately $6,500,000. That is the essence of the scheme—the misuse of reversionary settlements to enrich counsel at the expense of the class.

Whenever class counsel opt for a reversionary settlement with the intention of claiming 33⅓% of the gross nominal settlement fund in fees, they are *knowingly* sacrificing the interests of the class to obtain personal financial benefit. *It is a mathematical certainty* that any time class counsel seeks a fee of 33⅓% of a reversionary fund the requested fee will be 200% of what the class will receive. Subtracting 33⅓% from the reversionary fund for class counsel's fees leaves a maximum of 66⅔% of the fund for the class. Class counsel

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[1] In a "reversionary" settlement attorneys' fees and costs are first deducted from the gross settlement fund. Class members who file qualifying claims receive a percentage of the remaining fund based upon the assumption—which is a fiction—that 100% of the class will file qualifying claims. The interests of all class members who do not file qualifying claims revert to the settling defendants. Typically only 25% of the class files qualifying claims; 75% of the remaining fund then reverts to the defendants. This is in contrast with a "pro rata" settlement where the entire settlement fund, after payment of class counsel's fees and expenses, is paid out to qualifying claimants. There is no reversion to the settling defendants in a pro rata settlement. Even if only 25% of the class file claims, in a pro rata settlement these qualifying claimants get the entire remaining fund.

knows that only 25% of the class will file qualifying claims. This means that only 16⅔% of the fund will be disbursed to the class (*i.e.*, 25% of 66⅔%). Thus when class counsel seeks 33⅓% of the reversionary fund, it *knowingly* seeks a fee that is twice the 16⅔% of the fund actually paid to the class.

The Eleventh Circuit stated that the district court has unfettered discretion to "bas[e] the attorneys' fee award on the actual class recovery or on the gross settlement figure", *Waters v. International Precious Metals Corp.*, 190 F.3d 1291, 1298 (11th Cir. 1999); P.App., A-13 , and went on to hold that the district court did not abuse its discretion by awarding an attorneys' fee of 33⅓% of the gross settlement figure even though that amount was twice the amount that the class would receive.

The Eleventh Circuit's approach should be rejected for a number of different reasons. *First*, the "anything goes" approach of awarding fees based upon the gross settlement amount regardless of actual class recovery results in a misallocation of settlement funds, permitting class counsel to appropriate the larger part of the amount paid in settlement.

Second, it separates the interest of class counsel from that of the class by divorcing class counsel's compensation from the actual distribution to the class. It creates a powerful incentive for class counsel to opt for the reversionary form of settlement to enrich themselves at the expense of the class.

Once a reversionary form of settlement is used, defendants acquire an interest in the claims procedure, because that procedure determines the actual distribution and the reversion. In this case, class members were required to file a proof of claim and attach all of their monthly statements for the five-year class period. While not unusual for a reversionary settlement, this claims procedure reduced the number of qualified claimants. In a pro rata case, plaintiffs' counsel can adopt an automatic payment system reaching all members of the class. That is not possible in a reversionary settlement.

Third, the Eleventh Circuit's "anything goes" approach involves the federal courts in practices which undermine public confidence in the courts. There is typically no adversary presentation in proceedings leading to the approval of class action settlements. The settlement stipulation tends to be a rather complicated document. Pressed by the demands of their docket, district court judges rarely devote more than a few hours to the fairness hearing in a class action.

Fourth, this "anything goes" approach creates an unjustifiable difference between fees awarded in pro rata and those awarded in reversionary settlements, by permitting windfall fees in reversionary settlements. In a pro rata settlement, the fee necessarily bears a reasonable relationship to actual class recovery because the entire balance of the fund, after fees, is always paid to the class. For example, a 33⅓% fee in a pro rata case results in a class distribution of 66⅔% of the settlement fund; the fee is 50% of the class's recovery. *No court would ever permit a fee of 66⅔% of a pro rata fund.*

That, however, is precisely what the court endorses in a reversionary settlement when it awards a fee of 33⅓% of the gross amount *regardless of actual class recovery*. Perpetuation of the Eleventh Circuit's approach will guarantee that class counsel will choose reversionary settlements in order to claim disproportionately high fees.

The only effective way to eliminate these abuses of class settlements is to require that counsel's fees be limited to a reasonable percentage of the amounts actually distributed to the class in any tort case involving pecuniary loss. That rule is easy to apply. It can be readily understood by the public. Most importantly, that rule will eliminate the sordid spectacle of class actions yielding more in attorneys' fees than benefits to the class. That rule has already been adopted by Congress in the Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 77z-1(a)(6), and is applied in all securities class actions. There is no more reason to allow excessive attorneys' fees in a commodities action than there is in a securities action.

In any class action seeking a remedy for pecuniary loss, the amount actually distributed to the class is the definitive measure of the social value of the litigation. No public purpose is served by paying class counsel more than the amount of compensation received by the class.

Tying attorneys' fee awards to a reasonable percentage of the amounts actually distributed to the class will not unreasonably restrict the district court in awarding fair fees. The district court will be able to consider all of the special factors present in any case which warrant some higher or lower percentage of the amount received by the class.

Respondents make no effort to propose any rule, asking this Court to rubber-stamp whatever the district court decides, irrespective of the fee's relationship to the actual class benefit.

This case offers the Court a rare opportunity to eliminate these nefarious practices. Because of normally successful attempts by plaintiffs' counsel to silence defendants through clear sailing agreements, the Court is unlikely to have another such opportunity.

II. This Court should grant certiorari to resolve conflicting interpretations of *Boeing Co. v. Van Gemert*, 444 U.S. 472 (1980), which have led to conflicts below.

The decision of the Eleventh Circuit is based on its mistaken acceptance of the erroneous interpretation of *Boeing Co. v. Van Gemert*, 444 U.S. 472 (1980) urged by respondents. Respondents claim the *Boeing* decision "held that it was 'permissible' to base fees on the entirety of the fund". (Resp. at 23.) The Eleventh Circuit held that "[i]n *Boeing*, the Supreme Court rejected petitioner's argument that the attorneys' fee award could be based only on the portion of the common fund actually claimed by class members . . . ." 190 F.3d at 1294; P.App., A-6. Both are wrong. This Court did not purport to determine what fee should be paid in *Boeing*. All that *Boeing* decided was that the fee which had been awarded by the district court need not be deducted, in its

entirety, from the distributions made to claiming class members. The Court went on to say "we need not decide whether a class-action judgment that simply requires the defendant to give security against all potential claims would support a recovery of attorney's fees under the common-fund doctrine", thus expressly reserving decision as to reversionary funds. 444 U.S. at 480 n.5.

The Eleventh Circuit's opinion in this case conflicts with the opinion of the Ninth Circuit in *Williams v. MGM-Pathe Comm. Co.*, 129 F.3d 1026 (9th Cir. 1997) and the opinion of the Fifth Circuit in *Strong v. BellSouth Telecomm., Inc.*, 137 F.3d 844 (5th Cir. 1998). In this case, the Eleventh Circuit held:

> "Nothing in this opinion precludes a district court judge in a different case from basing the attorneys' fee award on the actual class recovery or on the gross settlement figure." (190 F.3d at 1298; P.App., A-13)

In *Williams*, the Ninth Circuit held:

> "We conclude that the district court abused its discretion by basing the fee on the class members' claims against the fund rather than on a percentage of the entire fund . . . ." (129 F.3d at 1027)

In the Eleventh Circuit, a district court judge can set a class counsel's fee based on the actual distribution; in the Ninth Circuit, she cannot. That's a conflict.

In this case, the Eleventh Circuit interpreted *Boeing* to "reject petitioner[s'] argument" that class action fees should be set in relation to the actual class distribution in reversionary settlements. In *Strong*, the Fifth Circuit held that *Boeing* did not apply to reversionary settlements, relying on the Supreme Court's express reservation in footnote 5 quoted above. 137 F.3d at 852 n.8. That's a conflict.

The Eleventh Circuit's permissive approach in this case has given rise to a conflict with serious practical results. In a

recent study conducted by National Economic Research Associates ("NERA") of securities class action in the federal courts and relied upon by the district court in this case, NERA concluded that attorneys' fees in securities class settlements in the Eleventh Circuit averaged 43% of the class distributions. (Pet. at 17.) Petitioners determined and placed on record two additional facts: (1) the settlement amounts in the NERA Study were all actually distributed to class members; and (2) no fee in any of those cases exceeded 50% of the actual class distribution.[2] That means that the fee awarded in this case, at over 200% of the actual distribution, was at least 400% of any fee ever awarded in the Eleventh Circuit in a securities class action settlement.

The NERA Study also concluded that average fees in the other federal circuits in securities class actions varied between 42.2% and 48.5% of class distributions. (Pet. at 4, 17.) The Eleventh Circuit's decision is thus in conflict with other circuits in its rationale and in conflict with district court decisions throughout the country in its results.

III. Respondents have offered no acceptable reasons for this Court to deny certiorari.

Respondents ask this Court to leave their exorbitant Fee Award undisturbed because they have allegedly incurred an "actual lodestar" of $12.6 million in this case. (Resp. at 20.) Respondents fail to disclose that the $12.6 million is not, in fact their actual lodestar. It is merely the result of multiplying their alleged but unexamined time expenditure by the rates which were in effect at the close of the litigation—rates which were materially higher than the actual rates during the years involved. The district court asked for no lodestar presentation and plaintiffs' counsel made none. Class counsel's guesstimate of time expenditures are notoriously unreliable. *See, e.g.,*

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[2] *See* Pet. at 17; App. K (NERA Study, Table 12b); App. M (Aff. of Michael R. Siebecker, executed April 21, 1997) at pp. M-4, ¶ 12; M-6, ¶ 15; and P.App., p.W-40.

Goldberger v. Integrated Resources, Inc., 2000 WL 320447 (2d Cir. March 28, 2000).

The fact that plaintiffs' counsel consumed seven years in pretrial proceedings and five months in trial time provides no measure of any value conferred by this litigation. The sole reason that this case consumed such resources is that plaintiffs' counsel *admittedly demanded $90,000,000 in cash up to the day before the settlement*, even though the alleged aggregate investment loss was only $120,000,000. As the NERA Study makes clear, securities class actions are settled for 2% to 10% of the investment loss. (P.App., W-26) In this case, that would be $4,000,000 to $12,000,000. The length of this case is the direct result of plaintiffs' counsel's unreasonable insistence on a $90,000,000 settlement. At the last moment, plaintiffs' counsel settled the case for a class distribution of $6,500,000. This case could have been settled for that amount years ago.

In the Eleventh Circuit, petitioners demonstrated at length that this case should never have been certified as a class action in the first place. It is no more than a glorified churning case and churning cases have never been certified as class actions because they require proof of individualized communications between individual customers and their brokers—in this case 20,600 customers and 800+ brokers. (P.App., W-12) The district court succeeded in transforming this case into a class action only by repealing the recognized reliance requirement from the securities laws in direct contravention of controlling Eleventh Circuit precedent. (P.App., W-14 to 18) Respondents made no attempt to defend the class certification decision in the Eleventh Circuit.

It is impossible to make any reasoned assessment of the justifiability of the highly unusual fee award in this case without dealing with the fact that this case should never have been prosecuted as a class action. Whether the fee claimed is said to be justified on "percentage of fund" or "lodestar" basis, any reviewing court must make some assessment of whether the case was a proper class action, particularly where the

district court's primary justification was its mistaken view that this was a "well-conceived class action". (P.App., W-4) The Eleventh Circuit simply refused to do so, dismissing that controlling factor without any consideration: "The merits of the underlying class action, notwithstanding the energy devoted to those topics by counsel, are not at issue in this appeal." 190 F.3d at 1292 n.1; P.App., A-2 n.1. The Eleventh Circuit's summary dismissal of that issue demonstrates that the panel simply abdicated its appellate responsibilities.

Respondents claim that they should be rewarded for creating the mere "opportunity" created by the reversionary fund and relieved of responsibility for the amount actually claimed, which they dismiss as a fortuity beyond their control. Their disclaimer of responsibility should be rejected. Plaintiffs' counsel control the form of class action settlements because defendants are interested in what settlements cost, not who gets the money.

Respondents could have opted for a pro rata settlement with an automatic payout to all class members. Instead, they chose a reversionary settlement so that they could claim a fee based on the gross nominal settlement fund. They adopted a claims procedure which required class members to submit a proof of claim and copies of all their monthly statements over the five-year class period. Seventy-five percent of the settlement fund consisted of ten-year notes bearing interest at a rate of 5.5%. Respondents initially claimed all of the cash, leaving the average class member with $66 per year in interest for 10 years, on a $1,200 note. The notice so advised the class, which is one of the reasons that only 25% of the class submitted qualifying claims. After the district court denounced their behavior as "outrageous" (P.App., W-38), respondents limited their demand to $5,000,000 in cash payable immediately after approval of the settlement. As a result, the average class distribution is $40.92 per year in interest on a ten-year note and $456 in cash. As respondents demonstrated in this case, plaintiffs' counsel do control the extent to which

class members can take advantage of the "opportunity", and should be held responsible for their behavior.

Respondents seek to deflect the Court's attention from the serious policy issues raised by petitioners by arguing that petitioners' agreement not to oppose plaintiffs' fee *application in the district court bars petitioners from appellate review.* The fact that petitioners agreed to submit the fee decision to the discretion of the district court, as limited by past precedent, is obviously no reason to deprive petitioners of their right to appellate review of an abuse of discretion which transgresses these limits.

The silence extorted by class counsel from defendants through clear sailing agreements over the past years has crippled effective appellate review. Clear sailing agreements serve no legitimate public purpose. They serve only to stifle the adversarial process to protect class counsel's fees from judicial scrutiny. The few appellate courts confronted with such agreements have refused to enforce them. *See, e.g.*, *Weinberger v. Great Northern Nekoosa Corp.*, 925 F.2d 518 (1st Cir. 1991); *Malchman v. Davis*, 761 F.2d 893 (2d Cir. 1985). Respondents' claim that petitioners bargained for and received a limitation on respondents' fee claim to 33⅓% in exchange for the clear sailing agreement is both ludicrous and false. Respondents may believe that they surrendered a significant right in foregoing a possible claim for 50% of the gross settlement fund. Petitioners do not. Respondents apparently believe that they might have received $20,000,000 (50% of $40,000,000) and the class $5,000,000 (25% of the remaining $20,000,000) but for their forbearance. Where clear sailing agreements are used to shield the kind of manipulation practiced below, they should be disregarded.

Respondents state that only one class member objected. However, the class notice never disclosed that the attorneys' fee would be twice the class recovery. If it had, there would doubtless have been numerous objections.

Unfortunately, respondents seek to deflect the Court's attention from the important issues raised by the Petition by a stream of false allegations. Respondents will not tax the Court's patience with any extended rebuttal apart from the following statements, supported by citation to the Appendix.

Petitioners never objected to any address location service which the Settlement Administrator proposed. (*See* P. App., X-33) Respondent's supporting citation makes no reference to any locator service. (*Compare* Resp. at 12 & RA-246a-2476a)

Finally, respondents' extravagant allegations about the nature of petitioners' business should be assessed in light of respondents' decision to settle the case for $6,500,000 or five cents on the dollar, on the eve of closing arguments after the district court had said that plaintiffs had "just barely" survived defendants' Rule 50 motions and expressed doubts as to whether plaintiffs had proven the scheme they had alleged. As plaintiffs' counsel told the court, they became concerned over the prospect of a "defense verdict" or "hung jury" and concluded that ". . . it's possible two weeks from now we'll have nothing for them . . . ." (P.App., W-27) As matters turned out, they had a little for the class, and a lot for themselves.

May 8, 2000

Respectfully submitted,

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